

THE HONORABLE MARSHA J. PECHMAN

UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF
WASHINGTON

EMMA ALVARADO, individually and on
behalf of all others similarly situated,

Plaintiff,

v.

MICROSOFT CORPORATION, a
Washington corporation; and DOES 1 through
100, inclusive,

Defendants.

NO. C09-189 MJP

PLAINTIFF'S RESPONSE TO
DEFENDANT MICROSOFT
CORPORATION'S MOTION TO
DISMISS SECOND AMENDED
COMPLAINT

PLAINTIFF'S RESPONSE TO DEFENDANT
MICROSOFT CORPORATION'S MOTION TO
DISMISS SECOND AMENDED COMPLAINT
CASE No. C09-0189 MJP

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I. INTRODUCTION

Defendant Microsoft Corporation (“Microsoft”) begins its motion to dismiss by asserting that Plaintiff’s Second Amended Complaint (“SAC”) “plead(s) around the indirect purchaser rule announced in *Blewett v. Abbott Laboratories*, 86 Wn. App. 782, 938 P.2d 842 (1997)” (Motion at 1:2-4) and, indeed, Microsoft is correct in this assertion. After reviewing Microsoft’s motion to dismiss the First Amended Complaint, Plaintiff was concerned that Microsoft misunderstood the basis for her claims and wished to avoid similar confusion on the part of the Court. As a result, Plaintiff volunteered to file a Second Amended Complaint in order to clarify the basis for her claims and eliminate the apparent confusion on Microsoft’s part. Unfortunately, notwithstanding Plaintiff’s best efforts in this regard (including the elimination of her anti-competition claim under the Unfair Business Practices Act, the deletion of all charging allegations related to anti-competitive conduct, Microsoft still seems to think (or wants the Court to believe for purposes of its motion to dismiss) that Plaintiff is alleging that Microsoft has engaged in anti-competitive activities that have resulted in charges being passed through to her as an indirect purchaser of a Microsoft product. But, that is not what Plaintiff alleges, and that is not what this case is about at all.

In this case, Plaintiff was the purchaser of a personal computer (“PC”) from Lenovo, an original equipment manufacturer (“OEM”). Plaintiff’s preferred operating system for her PC was Microsoft Windows XP (“Windows XP”). Microsoft mandated that in order for Plaintiff to obtain Windows XP she must first purchase a PC with the most current version of its Microsoft operating system – in Plaintiff’s case, the Windows Vista Business operating system (“Vista Business”) – and then “downgrade” to Windows XP. “Downgrade rights” are an end-user right and are documented in Microsoft’s End-User License Agreement (“EULA”) for Vista. Therefore, only after Plaintiff accepted the EULA for Vista Business did she become eligible to exercise her right to downgrade to Windows XP. In short, Plaintiff accepted the terms of the EULA for Vista not because she wanted to, but because she was required to do so

1 in order to be able to “downgrade” to the operating system that she actually wanted – namely,
 2 Windows XP. As a result, Plaintiff was forced to effectively “purchase” (technically,
 3 “license”) two operating systems for her PC when she only needed and/or wanted one. And, to
 4 make matters worse, Plaintiff was forced to purchase/license a premium, more expensive
 5 version of the operating system that she never wanted in the first place (Vista Business) in
 6 order to be able to downgrade to the operating system that she wanted (Windows XP).

7 Microsoft’s undisputed monopoly position in the PC software market has enabled it to
 8 force Plaintiff (and millions of other consumers) to make this needlessly duplicative and
 9 unnecessary purchase of software. However, Plaintiff is not alleging a vertical price-fixing
 10 conspiracy that results in an overcharge being “passed through” to “indirect purchaser”
 11 consumers by direct purchaser retailers or distributors as occurred in *Blewett*. Rather, Plaintiff
 12 alleges that Microsoft’s conduct constitutes an unfair business practice that is injurious to
 13 consumers because it: (1) forces consumers to purchase two operating systems when they only
 14 need and/or want one; and (2) results in unnecessary retail price inflation in the market for
 15 PCs. That is what Plaintiff alleges, and that is what this case is all about. That is what Plaintiff
 16 alleges, and that is what this case is all about.

17 II. STANDARD OF REVIEW

18 Microsoft has moved to dismiss the Second Amended Complaint under Rule 12(b)(6) of
 19 the *Federal Rules of Civil Procedure* for failure to state a claim upon which relief may be
 20 granted. In deciding a Rule 12(b)(6) motion, the Court must accept the complaint’s allegations
 21 as true and construe them in the light most favorable to the nonmoving party. *Hansen v.*
 22 *Department of the Treasury*, 528 F.3d 597, 599 (9th Cir. 2007). “The issue is not whether a
 23 plaintiff will ultimately prevail but whether the claimant is entitled to offer evidence to support
 24 the claims. Indeed it may appear on the face of the pleadings that a recovery is very remote and
 25 unlikely but that is not the test.” *Swartz v. KPMG, LLP*, 476 F.3d 756, 763 (9th Cir. 2007).
 26

1 Recently, the United States Supreme Court has issued two decisions clarifying the
 2 standards to be applied by the district courts in ruling on motions to dismiss under Rule
 3 12(b)(6). In *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), the Supreme Court
 4 concluded that “[d]ismissal is appropriate where a complaint fails to allege enough facts to state
 5 a claim to relief that is plausible on its face.” *Id.* at 570. Correspondingly, in *Ashcroft v. Iqbal*,
 6 --- U.S. ----, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009), the Supreme Court explained that a
 7 complaint withstands the plausibility test “when the plaintiff pleads factual content that allows
 8 the court to draw the reasonable inference that the defendant is liable for the conduct alleged.”
 9 *Id.* 129 S. Ct. at 1949, citing *Twombly*, 550 U.S. at 556.; *see also Moss v. U.S. Secret Serv.*, 572
 10 F.3d 962, 969 (9th Cir. 2009) (citing *Iqbal*, 129 S.Ct. at 1949) (“In sum, for a complaint to
 11 survive a motion to dismiss, the nonconclusory ‘factual content,’ and reasonable inferences
 12 from that content, must be plausibly suggestive of a claim entitling the plaintiff to relief.”). As
 13 demonstrated herein, the allegations in Plaintiff’s Second Amended Complaint satisfy the
 14 plausibility standards enunciated by the courts in *Twombly*, *Iqbal* and *Moss*.

15 III. STATEMENT OF FACTS

16 Plaintiff purchased a Thinkpad X61 laptop computer from Lenovo, for her own
 17 personal use and not for resale. To obtain the Windows XP operating system that she wanted
 18 on her laptop, Plaintiff was required to purchase a computer that included a license for Vista
 19 Business – one of Microsoft’s most expensive operating systems and one that Plaintiff did not
 20 need or desire – in order to “downgrade” to Windows XP Professional. (SAC, ¶ 4.)

21 Microsoft is a computer technology corporation that develops, manufactures, licenses,
 22 and supports a wide range of software products for PCs. Microsoft’s flagship products, the
 23 Windows operating systems, are used on more than 90 percent of Intel-based PCs, the
 24 dominant type of PC in the United States. The operating system is the most important program
 25 on a PC. Every PC must have an operating system to run other programs. (SAC, ¶ 8.)
 26 Microsoft possesses (and for several years has possessed) monopoly power in the market for

1 PC operating systems. See, *United States v. Microsoft Corp.*, 87 F. Supp. 2d 30 (D.D.C. 2000);
 2 *New York v. Microsoft Corp.*, 209 F. Supp. 2d 132 (D.D.C. 2002).

3 The primary channel through which Microsoft distributes its Windows operating
 4 systems is pre-installation on new PCs by PC manufacturers (referred to as "OEMs"). Because
 5 a PC can perform virtually no useful tasks without an operating system, OEMs consider it a
 6 commercial necessity to preinstall an operating system on the PCs they sell. And because there
 7 is no viable competitive alternative to the Windows operating system for PCs, OEMs consider
 8 it a commercial necessity to preinstall Windows operating systems on their PCs. (SAC, ¶ 9.)

9 Both OEMs and Microsoft recognize that consumers have no commercially viable
 10 substitute for Windows, and OEMs cannot preinstall Windows on their PCs without a license
 11 from Microsoft. Because nearly all PCs in the United States are shipped with a copy of
 12 Windows preinstalled, *Microsoft has dictated the terms of the use of its Windows operating*
 13 *systems by consumers – referred to as “End Users” – through its End User License*
 14 *Agreements (“EULA”) and imposes licensing terms that restrict which versions of Windows*
 15 *may be sold on PCs.* (SAC, ¶ 10.)

16 On or about January 30, 2007, Microsoft publicly released the first version of the
 17 Windows Vista operating system (“Vista”) – the long-awaited successor to the Windows XP
 18 operating system. During the succeeding two years, Microsoft released multiple versions of
 19 Vista – including Vista Home Premium, Vista Business and Vista Ultimate. Vista Business
 20 and Vista Ultimate are higher-priced versions of Vista that include specialized applications.
 21 Vista Business costs up to \$100 more than Vista Home Basic; Vista Ultimate costs up to \$200
 22 more than Vista Home Basic. (SAC, ¶ 29.)

23 When Microsoft first launched Vista, it required OEMs to pre-install Vista onto their
 24 PCs and to sell the PCs to consumers for a single price that included the pre-installed Vista. As
 25 the sole licensor of Vista, Microsoft enjoys vast power over OEMs. As a result, during the
 26

1 initial period of time after Vista's launch, Microsoft forced OEMs to significantly curtail their
2 sales of PCs pre-installed with the Windows XP. (SAC, ¶ 30.)

3 The public's reaction to the launch of Vista was not favorable. Consumers reported
4 numerous problems using Vista, and these problems were and continue to be widely publicized
5 in various media outlets. Among the problems cited have been Vista's heavy horsepower
6 requirements, its intrusive security measures and its incompatibility with older legacy
7 applications. In response to the public's dissatisfaction with Vista, Microsoft decided to grant
8 consumers who purchased a new PC with Vista the right to "downgrade" the operating-systems
9 software from Vista to Windows XP. (SAC, ¶ 31.)

10 Initially, Microsoft made this "downgrade" right from Vista available to consumers for
11 a limited period of time, then until June 30, 2008. Subsequently, Microsoft extended the time
12 period until January 31, 2009, then until July 31, 2009, and then until October 21, 2009 – that
13 is, until the time that Microsoft replaced Vista with Windows 7. Microsoft has continued the
14 same "downgrade rights" scheme with Windows 7, under the moniker "Windows 7 Downgrade
15 Rights," effective from October 22, 2009 until at least April 1, 2011. (SAC, ¶¶ 14, 32.)

16 Microsoft's "downgrade rights" policies state: "The right to downgrade is an end-user
17 right [documented in the EULA]...The End User must provide the downgrade media and a
18 valid Product Key..." These policies also state that: "A System Builder (when authorized by
19 the end user), or the end user [may install the Downgrade Software [for Windows XP]].

20 *Because downgrade rights are an end user right granted in the end user license agreement*
21 *(EULA), the end user must first be able to accept the EULA associated with the software [Vista,*
22 *and now Windows 7], so this software must be installed first before the Downgrade Software is*
23 *installed."* (SAC, ¶ 33.) This process is further defined in Microsoft's Desktop Operating
24 System License Agreement ("DTOS"). The downgrade media [Windows XP] must be
25 supplied to the OEM by the End User and must come from a legally licensed version of
26 Microsoft retail, OEM/System Builder, or Volume License channels. (SAC, ¶ 12.)

1 Although many consumers would prefer to purchase a new PC pre-installed with
 2 Windows XP or at least not pre-installed with Vista or Windows 7, Microsoft has used its
 3 monopoly position in the PC operating systems market to take advantage of consumer demand
 4 for Windows XP by requiring consumers to purchase a PC that includes a license for the use of
 5 Vista or Windows 7 and to pay money to downgrade to Windows XP Professional, using
 6 downgrade media provided by the consumer at the consumer's cost. To make matters worse,
 7 Microsoft requires consumers to purchase a PC that includes a license for either Vista Business
 8 or Vista Ultimate – and now Windows 7 Professional or Windows 7 Ultimate – versions of the
 9 operating systems that: (a) are premium, more expensive versions of the home versions of the
 10 same operating systems: and (b) include specialized applications that are neither needed nor
 11 wanted by an ordinary consumer seeking to purchase a PC primarily for personal, non-business
 12 use. (SAC, ¶ 34.)

13 Plaintiff alleges that Microsoft conceived and implemented the “right” for consumers to
 14 “downgrade” to Windows XP Professional in order to: (a) maintain and/or inflate its sales
 15 figures for, and profits from, sales of Vista and Windows 7 (particularly the Vista Business,
 16 Vista Ultimate, Windows 7 Professional and Windows 7 Ultimate versions) because Microsoft
 17 includes in its sales figures all sales of pre-installed Vista and Windows 7 – even those that, at
 18 the time of sale to the End User/consumer, have been “downgraded” to Windows XP
 19 Professional and thus never were used or intended to be used by the consumer; and (b) recoup
 20 its investment in developing and producing Vista and Windows 7 by forcing consumers to
 21 purchase the premium, more expensive versions of Vista and Windows 7 (Vista Business, Vista
 22 Ultimate, Windows 7 Professional, and Windows 7 Ultimate) in order to “downgrade” to
 23 Windows XP. (SAC, ¶¶ 32, 35.)

24 In response to the high demand for downgrades, Microsoft eventually permitted its
 25 OEMs to perform downgrades for the End User/consumer by installing Windows XP directly at
 26 the factory. OEMs have charged consumers a range of fees to cover the full cost of the

1 downgrading. For example, in December 2008, Dell was charging consumers a total of \$150 to
 2 downgrade from Vista Home Premium to Windows XP Professional. When challenged
 3 regarding the reasonableness of the amount of its downgrade fee, Dell responded that only \$20
 4 of the fee was attributable to the actual price of Windows XP. The other \$130 was the cost of
 5 complying with Microsoft's requirement that, prior to downgrading to Windows XP
 6 Professional, the standard Vista operating system first must be replaced with either Vista
 7 Business or Vista Ultimate. In other words, prior to permitting the consumer to "downgrade"
 8 to Windows XP Professional, Microsoft first mandates that the consumer "upgrade" from the
 9 basic versions of Vista or Windows 7 to Vista Business, Vista Ultimate, Windows 7
 10 Professional or Windows 7 Ultimate – thereby forcing the consumer to incur an unnecessary
 11 expense and creating revenue for Microsoft by virtue of the End User/ consumer purchasing
 12 two operating systems for one PC. (SAC, ¶ 36.)

13 The PC operating systems market is estimated to be worth more than \$50 billion
 14 annually in the U.S. alone. As of October 2009, Microsoft controlled approximately 90 percent
 15 of that market. On July 18, 2008, Microsoft announced that it had sold more than 180 million
 16 Vista licenses, which equates to gross sales revenues of between 30 and 60 billion dollars from
 17 Vista licenses. These figures include Vista licenses that have been downgraded to Windows
 18 XP. (SAC, ¶ 38.)

19 During the past two years, approximately 35 percent of the consumers purchasing a new
 20 PC have paid to downgrade the operating system from Vista to Windows XP. In doing so,
 21 consumers have been forced by Microsoft to purchase two operating systems – one for which
 22 they have no use and likely will never use (Vista) and one which they desire to use (Windows
 23 XP) but are forced to obtain via a "downgrade." And because Microsoft has mandated that
 24 downgrade "rights" apply only to Vista Business and Vista Ultimate (and now Windows 7
 25 Professional and Windows 7 Ultimate), Microsoft's mandate has artificially inflated the demand
 26 for Vista Business and/or Vista Ultimate by approximately 54 percent, attributable to those

1 consumers who purchased Vista Business or Vista Ultimate solely to be able to downgrade to
 2 Windows XP. The same will hold true for Windows 7 Professional and Windows 7 Ultimate.
 3 (SAC, ¶ 39.)

4 Plaintiff and the other members of the Class have suffered injury to their property as a
 5 result of Microsoft's unfair downgrade rights scheme because they have been forced to
 6 purchase Vista or Windows 7 in order to obtain and use the Windows XP. As a result, Plaintiff
 7 and the other members of the Class are forced to pay more for a PC than they otherwise would
 8 have to pay due to the retail price inflation that is directly attributable to Microsoft's
 9 requirement that the End User/consumer purchase two operating systems for one PC. (SAC,
 10 ¶ 40.)

11 Plaintiff and the other members of the Class also have suffered injury to their business
 12 and property as a result of Microsoft's unfair downgrade rights scheme because, owing to
 13 Microsoft's undisputed monopoly position in the PC operating systems market, they have been,
 14 and continue to be, forced to pay substantially more to acquire Windows XP than they would
 15 have to pay in a competitive marketplace in which there were available alternative PC
 16 operating systems. (SAC, ¶ 41.)

17 IV. ARGUMENT

18 A. The Indirect Purchaser Rule Does Not Bar Plaintiff's Claims

19 1. Microsoft imposed its unfair "downgrade rights" scheme directly on Plaintiff 20 and the other class members through its EULA

21 Microsoft imposed its EULA for Vista directly on Plaintiff, who was required to agree
 22 to its terms in order to obtain and use Windows XP. Plaintiff had little choice but to do so,
 23 given Microsoft's dominating position in the PC operating systems market and her need for an
 24 operating system on her PC. Microsoft's unilaterally imposed EULA forced Plaintiff to
 25 purchase a premium version of Vista before purchasing and installing Windows XP.
 26

1 Although Microsoft argues that Plaintiff indirectly purchased her operating systems and
 2 associated licenses from the OEM, Microsoft cannot deny that it imposed its EULA directly on
 3 Plaintiff. That EULA is a contract between Microsoft and Plaintiff. The OEM is not a party to
 4 the EULA. Consumers such as Plaintiff enter into the EULA with Microsoft by hitting the “I
 5 accept” tab when configuring their PCs after purchase. Plaintiff had no choice but to accept
 6 Microsoft’s terms. Otherwise, her PC would have no operating system and would not function.
 7 The downgrade media [Windows XP] must be supplied to the OEM by the End User and must
 8 come from a legally licensed version of Microsoft retail, OEM/System Builder or Volume
 9 License channels. (SAC, ¶ 12.) Thus, Microsoft imposed its unfair downgrade rights scheme
 10 *directly* on Plaintiff through its EULA – *not indirectly* through the OEM.

11 2. The indirect purchaser rule applies to fixed prices – not forced purchases

12 Microsoft argues that *Blewett v. Abbott Laboratories*, 86 Wn. App. 782, 938 P.2d 842
 13 (1997) bar Plaintiff’s claims in this action – irrespective of how Plaintiff alleges them –
 14 because Plaintiff is an indirect purchaser of the Microsoft software at issue. However, the facts
 15 of *Blewett*, when juxtaposed with the facts underlying Plaintiff’s claims, demonstrate that
 16 *Blewett* is distinguishable and therefore not controlling.

17 In *Blewett*, the plaintiff alleged that major drug manufacturers acted under a mutual
 18 understanding (*i.e.* conspiracy) to sell drugs to local pharmacies at higher prices than they sold
 19 the same drugs to HMO outlets and mail-order pharmacies. The plaintiff claimed that the
 20 defendant manufacturers’ acts resulted in illegal overcharges for prescription brand-name drugs
 21 purchased from local pharmacies and drug stores. The plaintiff further alleged that the
 22 discriminatory pricing scheme was not justified by differences in costs, sales methods, or
 23 quantities sold, and therefore constituted horizontal price fixing. The plaintiff brought claims
 24 against the manufacturers for (1) an unfair combination in restraint of trade, in violation of the
 25 Washington Consumer Protection Act (the Act), RCW 19.86.030, and (2) an unfair trade
 26 practice, in violation of RCW 19.86.020. *Id.* at 784.

1 The *Blewett* court examined *Illinois Brick Co. v. Illinois*, 431 U.S. 720 (1977), and held
 2 that indirect purchasers of price-fixed goods do not have standing to sue for antitrust violations
 3 under the Act. 86 Wn. App. at 786-88. The *Blewett* court cited the three policy reasons
 4 articulated in *Illinois Brick*:

- 5 ▪ First, allowing direct purchasers to recover for the full
 6 overcharge concentrates their claims, resulting in more
 7 rigorous private enforcement of the antitrust laws.
- 8 ▪ Second, forbidding suits by indirect purchasers avoids
 9 the evidentiary complexities and uncertainties in proving
 10 the passing on of injuries in the real economic world
 11 rather than an economist's hypothetical model.
- 12 ▪ Third, forbidding suits by indirect purchasers protects
 13 defendants from multiple liability to indirect and direct
 14 purchasers.

15 *Id.* at 785-86.

16 In *Blewett*, the plaintiff indirectly purchased the overpriced drugs from the pharmacies –
 17 not from the drug manufactures. Thus, the plaintiff lacked standing to sue for a combination in
 18 restraint of trade under RCW 19.86.030. *Id.* at 789. The *Blewett* court also held that the
 19 plaintiff's unfair-trade-practice claim under RCW 19.86.020 was a restraint of trade claim
 20 under a different label and, therefore, similarly barred. *Id.*

21 Here, by contrast, Plaintiff does not allege price fixing that results in an overcharge
 22 being passed through to her as the end use, "indirect" purchaser. Rather, Microsoft forces end-
 23 user consumers to purchase one operating system (Vista) in order to be able to downgrade to
 24 the operating system (Windows XP) that the consumer actually wants. In this sense,
 25 Microsoft's conduct is analogous to a drug manufacturer forcing consumers to buy an
 26 unwanted and unneeded drug in order to obtain the medication that they actually need and
 want.

3. Plaintiff's "direct" purchase of her PC does not bar her claims

Microsoft's argument that Plaintiff directly purchased her PC – and her operating-system license – from the OEM and, by inference, therefore, purchased her operating system license from Microsoft "indirectly" is simply incorrect. The OEM preloaded Plaintiff's PC with an operating system subject to Microsoft's EULA. But, the EULA had no validity until Plaintiff accepted its terms, and the OEM was not a party to the EULA. In fact, Microsoft's "downgrade rights" policies explicitly excludes the OEM as a party:

The right to downgrade is an end-user right [documented in the EULA]...The End User must provide the downgrade media and a valid Product Key...A System Builder (when authorized by the end user), or the end user [may install the Downgrade Software [for XP]]. Because downgrade rights are an end user right granted in the end user license agreement (EULA), the end user must first be able to accept the EULA associated with the software [Vista, and now Windows 7], so this software must be installed first before the Downgrade Software is installed.

(SAC, ¶ 33.)

This process is further defined in Microsoft's DTOS. The downgrade media [Windows XP] must be supplied to the OEM by the End User and must come from a legally licensed version of Microsoft retail, OEM/System Builder, or Volume License channels. (SAC, ¶ 12.)

Microsoft's EULA makes clear that the end user must *first* accept the EULA associated with the unwanted operating system (Vista or Windows 7). Microsoft thus forces the end user to *first* purchase and install Vista or Windows 7 before obtaining and installing Windows XP. Consequently, the three *Illinois Brick* policy reasons cited by *Blewett* do not apply to the facts of this case given that:

- First, only Plaintiff (not the OEM) suffered damages by having to pay for two operating systems. Microsoft *directly* imposed its downgrade scheme in its EULA on Plaintiff – not on the OEM. End users such as Plaintiff suffer the full measure of damages from Microsoft's unfair downgrade rights scheme and are the logical parties to rigorously enforce the RCW.

- 1 ▪ Second, Plaintiff's damages are not hypothetical or complex. Microsoft,
2 through its EULA, forced Plaintiff to pay for two operating systems. This was
3 not a passed-on injury.
- 4 ▪ Third, Microsoft is not potentially liable both to Plaintiff and to the OEM. *The*
5 *OEM does not have standing to sue because it is not a party to the EULA, and*
6 *suffered no resulting damage.* If Plaintiff cannot sue, then nobody can.

7 **B. Plaintiff Has Stated A Claim For Unfair Business Practices Under The**
8 **Washington Consumer Protection Act**

- 9 1. The Washington Consumer Protection Act Independently Prohibits Unfair Acts
10 or Practices Without the Requirement of Deception

11 The Washington Consumer Protection Act ("CPA") broadly prohibits any unfair or
12 deceptive acts or practices. *See* RCW 19.86.020. To state a CPA claim, a plaintiff must show:
13 (1) that the defendant engaged in an unfair or deceptive act; (2) that the act occurred in the
14 conduct of the defendant's trade; (3) that the practice affected the public interest; (4) that the
15 plaintiff was injured; and (5) that the defendant's act or practice was the proximate cause of the
16 plaintiff's injury. *Hangman Ridge Training Stables, Inc. v. Safeco Title Ins. Co.*, 105 Wn.2d
17 778, 787-93, 719 P.2d 531 (1986). Here, Microsoft wrongly asserts that Plaintiff has not
18 established the first prong of the *Hangman Ridge* test – namely, that Microsoft engaged in an
19 unfair or deceptive act.

20 As Microsoft's own authority clearly establishes, to be actionable under the CPA, a
21 practice need not be both "unfair" and "deceptive", as each provides an independent ground for
22 a claim for relief under the CPA. *See Watkins v. Peterson Enters., Inc.*, 57 F. Supp. 2d 1102,
23 1111 (E.D. Wash. 1999) (noting that the terms unfair and deceptive are separate concepts). In
24 fact, Washington courts have found that "[t]he universe of 'unfair' business practices is broader
25 than, and encompasses, the universe of 'deceptive' business practices." *Panag v. Farmers Ins.*
26 *Co. of Washington*, 166 Wn.2d 27, 51, 204 P.3d 885 (2009). Because Plaintiff need not
 establish that a practice is deceptive in order to state a CPA claim, Microsoft's assertion that
 Plaintiff's Second Amended Complaint "contains only a single conclusory allegation of
 deception" is irrelevant. (Motion at 12:20-25.) Plaintiff's CPA claim is not predicated on

1 consumers being *deceived*; rather, it is predicated on the *unfairness* of Microsoft's business
2 practice.¹

3 Under Washington law, a practice is unfair if it: (1) causes substantial injury to the
4 consumer; (2) is not outweighed by countervailing benefits to consumers or competitors; and
5 (3) is not reasonably avoidable by the consumer. *See Panag*, 166 Wn.2d at 51 (citing *Camacho*
6 *v. Auto Club of S. Cal.*, 142 Cal. App. 4th 1394, 48 Cal. Rptr. 3d 770 (2006)); *see also*
7 Statements of General Policy or Interpretation Staff Commentary on the Fair Debt Collection
8 Practices Act, 53 Fed. Reg. at 50,097, 50,107 (Dec. 13, 1988)). In this case, Plaintiff's Second
9 Amended Complaint plainly sets forth facts demonstrating that Microsoft's conduct is an unfair
10 business practice.

11 a. *Substantial Injury*

12 "In most cases a substantial injury involves monetary harm, as when sellers coerce
13 consumers into purchasing unwanted goods or services." *See* FTC's 1980 Policy Statement at
14 3, 104 F.T.C. 949, 1070 (1984); codified in a 1994 amendment to 15 U.S.C. § 45(n). In the
15 Second Amended Complaint, Plaintiff alleges that Microsoft coerced her into buying the Vista
16 or Windows 7 operating system so that she could then downgrade to the Windows XP
17 operating system, thereby forcing her to purchase two operating systems for her PC when she
18 only needed and/or wanted one. (SAC, ¶¶ 34, 37, 40, 45, 46, and 48.) Plaintiff further alleges
19 that Microsoft forced consumers to purchase the more expensive or "premium" version of the
20 Vista or Windows 7 operating system in order to be able to downgrade to Windows XP. (SAC,
21 ¶¶ 34, 36, 39, 41, 45, 46, and 48.) This conduct injured Plaintiff because it forced her to
22 purchase two operating systems when she only needed and wanted one.

23
24 ¹ Moreover, despite Microsoft's assertions to the contrary, Plaintiff does not allege a *per se* violation of the CPA
25 (which eliminates Microsoft's argument at B.2 in its Motion at 13:8-19) nor does she allege an antitrust claim
26 tying the "unfair" practice to unfair competition (which eliminates Microsoft's arguments relating to anti-
competitive conduct discussed at B.3. in its Motion at 14:13-17:9). Plaintiff does not accuse Microsoft of using its
monopoly position to set monopolistically high prices. In fact, Plaintiff *does not take issue with the prices of Vista*
or Windows XP. She takes issue with having to buy both when she only needs one.

b. *Countervailing Benefits*

There are no countervailing benefits to consumers or competition that outweigh Microsoft's unfair conduct. In fact, even Microsoft does not assert that there are *any* countervailing benefits to consumers or competition from this practice.

c. *Reasonable Avoidance*

Finally, consumers could not reasonably have avoided injury from Microsoft's conduct. Microsoft required Plaintiff to purchase Vista in order to downgrade to the Windows XP. (SAC, ¶46.) It was Microsoft's mandate that caused the injury to Plaintiff's property, and there was no reasonable means for Plaintiff to avoid the injury.

For all of the above reasons, Plaintiff has stated a claim for relief under the CPA's "unfairness" prong.

2. Microsoft's Downgrade Rights Scheme Independently Violates the CPA Because it Causes Retail Price Inflation

In addition to Plaintiff's claim that Microsoft's practice of forcing consumers to purchase two operating systems is generally unfair and a violation of the CPA, Plaintiff also avers that Microsoft's practice led to retail price inflation of the Vista operating system software which is an independent violation of the CPA.

As this court recognized in *Kelley v. Microsoft Corp.*, 251 F.R.D. 544, 559 (W.D. Wash. 2008), a CPA claim can be asserted where a plaintiff alleges that s/he paid more for a product than s/he otherwise would have paid, but for the artificially created demand by the defendant. Here, as in *Kelley*, Microsoft artificially created an increased demand for Vista by forcing consumers to purchase Vista when they did not want or need it. This conduct artificially inflated the demand for Vista Business and/or Vista Ultimate by approximately 54 percent. (SAC, ¶ 39.)

Plaintiff's Second Amended Complaint sets forth facts demonstrating that Microsoft's retail price inflation scheme is unfair because: (1) it caused substantial injury; (2) there are no

1 countervailing benefits; and (3) Plaintiff could not reasonably avoid the injury. *See Panag*, 166
 2 Wn.2d at 51. With regard to the “substantial injury” element, Microsoft’s conduct results in
 3 retail price inflation because it artificially increases sales of the Vista – sales that would not
 4 have occurred but for Microsoft’s requirement that consumers purchase the Vista in order to
 5 downgrade to Windows XP. (SAC, ¶¶ 39-40.) This scheme resulted in substantial injury to
 6 Plaintiff because she paid more for a PC than she would have otherwise paid absent the retail
 7 price inflation. (SAC, ¶¶ 37 and 40.) No countervailing benefits to consumers or competition
 8 outweigh Microsoft’s unfair conduct that creates this retail price inflation. Again, Microsoft
 9 does not assert *any* countervailing benefits to consumers or competition from the retail price
 10 inflation. Rather, Microsoft simply forced Plaintiff to pay more than she otherwise would have
 11 paid. (SAC, ¶ 48.) Finally, Plaintiff could not have reasonably avoided the effect of the retail
 12 price inflation because Microsoft required her to purchase Vista in order to downgrade to
 13 Windows XP. (SAC, ¶ 46.) Microsoft’s undisputed monopoly power prevented Plaintiff from
 14 purchasing an alternate operating system.

15 Plaintiff’s case is analogous to the *Kelley* case. In *Kelley*, this court found that common
 16 issues could predominate as to whether Microsoft’s “marketing campaign inflated demand
 17 market-wide.” *See Kelley v. Microsoft Corp.*, No. C07-0475, 2009 WL 413509, at 5 (W.D.
 18 Wash. Feb. 18, 2009). Plaintiff is aware that this court decertified the class in *Kelley*, but notes
 19 that the individual CPA claim still stands. *Id.* at 9. Here, as in *Kelley*, Plaintiff paid more for a
 20 PC than she otherwise would have paid, but for Microsoft’s scheme, thereby resulting in
 21 “retail-price inflation.” (SAC, ¶¶ 37 and 40.)

22 For these reasons, Plaintiff has stated a claim for retail price inflation as an independent
 23 CPA violation. Therefore, Microsoft’s motion to dismiss the CPA claim should be denied.

24 3. The Court Should Reject Microsoft’s Other Erroneous Arguments

25 Microsoft maintains that anti-competitive conduct that does not violate the antitrust
 26 provisions of the CPA cannot be actionable as “unfair.” (Motion at 14:22-23.) Microsoft

1 provides no legal authority for this proposition. Instead, Microsoft relies on a legislative
2 declaration that “anti-competitive conduct is unfair,” providing no support for its subsequent
3 conclusion that anti-competitive conduct is the only conduct actionable as unfair under the
4 CPA. Here, Plaintiff simply alleges that Microsoft engaged in a pattern of conduct that was
5 unfair to consumers and thus violates the Washington CPA. (SAC, ¶¶ 42-50.) Plaintiff does
6 not allege that Microsoft’s practices were in and of themselves anti-competitive, merely that
7 Microsoft’s undisputed monopoly power allows it to perpetuate this unfair practice because
8 consumers cannot take their business elsewhere.

9 For these reasons, Microsoft’s reliance on cases in which courts have found that
10 monopolies are free to choose the parties with whom they will deal is misplaced. (Motion at
11 15:4-23.) For example, in *Consolidated Dairy Prods. Co. v. Bar-T Ranch Dairy, Inc.*, 97
12 Wn.2d 167 (1982), the Washington Supreme Court held that being a monopoly “does not, in
13 itself, cast any cloud upon their right to set the prices at which they were willing to sell.” *Id.* at
14 178. However, this statement has no bearing on Plaintiff’s allegations in this case because
15 Plaintiff is not quibbling with the price that Microsoft, as a monopolist, sets for its operating
16 systems. Rather, Plaintiff is claiming that it is unfair for Microsoft to force her to purchase two
17 operating systems when she only needs and/or wants one.

18 Microsoft also argues that forcing Plaintiff to buy two operating systems qualifies as
19 “routine market conduct” in phasing out an older operating system in favor of a new one.
20 However, Microsoft did not phase out Windows XP in favor of Vista. Rather, given the bleak
21 outlook for Vista sales, Microsoft clung onto Windows XP for dear life and forced consumers
22 to buy Vista in order to obtain Windows XP. This downgrade rights scheme has endured from
23 Microsoft’s introduction of Vista in January 2007 to the present, even with Windows 7
24 replacing Vista as Microsoft’s most current operating system.

25 The other legal authority cited by Microsoft is similarly distinguishable, as it all
26 addresses antitrust cases involving pricing practices.

Microsoft's attempt to convert Plaintiff's allegations into anti-trust and/or anti-competitive claims that are more easily dismissed under the Washington applicable to such claims should be rejected, and its motion to dismiss should be denied.

C. Plaintiff Has Stated A Claim For Unjust Enrichment

To state a claim for unjust enrichment under Washington law, a plaintiff must allege that: (1) the plaintiff conferred a benefit upon the defendant; (2) the defendant had an "appreciation or knowledge" of the benefit; and (3) retention of the benefit by the defendant would be unjust under the circumstances. *Balie Communications Ltd. v. Trend Bus. Sys. Inc.*, 61 Wn. App. 151, 160, 810 P.2d 12 (1991); *Kelley v. Microsoft Corp.*, 2009 WL 973368 at *5 (W.D. Wash. Apr 10, 2009). *See also* Restatement (First) of Restitution § 1 (1937). Microsoft challenges all three elements. However, the allegations in Plaintiff's Second Amended Complaint plainly satisfy all three of these elements.

1. Plaintiff Conferred a Benefit on Microsoft by Paying for an Operating System She Did Not Want or Need

Plaintiff alleges that Microsoft required her to purchase an operating system she neither wanted nor needed. (SAC, ¶¶ 4, 53.) Plaintiff further alleges that Microsoft benefitted both directly and indirectly as a result of its unfair scheme. (SAC, ¶¶ 36-38; 53.) In particular, Plaintiff alleges that she directly conferred a benefit on Microsoft by entering into the EULA and agreeing to a license for Vista. The EULA required Plaintiff to purchase the unwanted Vista operating system, resulting in increased revenues and profits for Microsoft. Plaintiff alleges that Microsoft has implemented a scheme which strictly controls when consumers may purchase Windows XP and that Microsoft's scheme resulted in consumers paying monies for operating systems (Vista and Windows 7) that they would not otherwise purchase. *Id.* Moreover, Plaintiff alleges that Microsoft's gross revenues include monies received for purchases of Vista licenses so consumers could downgrade to Windows XP. *Id.* These

1 allegations satisfy the first element of an unjust enrichment claim – namely, that Plaintiff
 2 conferred a benefit on Microsoft.

3 Contrary to Microsoft’s arguments, Plaintiff need not confer the benefit directly on
 4 Microsoft. Analyzing the common law of unjust enrichment from multiple jurisdictions with
 5 elements identical to Washington law, the federal district court in *In re Cardizem CD Antitrust*
 6 *Litig.*, 105 F. Supp. 2d 618 (E. D. Mich. 2000) found such arguments to be unpersuasive.
 7 “Whether or not the benefit is directly conferred on the defendant is not the critical inquiry;
 8 rather, the plaintiff must show that his detriment and the defendant’s benefit are related and
 9 flow from the challenged conduct.” *Id.* at 671. Similarly, in *Muehlbauer v. General Motors*
 10 *Corporation*, the court concluded that “an unjust enrichment claim may be premised on an
 11 indirect conferral of benefits.” *Muehlbauer*, 431 F. Supp. 2d 847, 853 (N.D. Ill. 2006)
 12 (analyzing unjust enrichment elements identical to a Washington claim). The court went on to
 13 find that “Plaintiffs say they purchased and leased vehicles manufactured by defendant, and by
 14 paying for those vehicles they conferred a benefit upon defendant. These allegations satisfy the
 15 first prong of an unjust enrichment claim.” *Id.* at 854 (citation omitted).

16 Likewise, in *Kreidler v. Pixler*, No. C06-0697RSL, 2006 WL 3539005 (W.D. Wash.
 17 Dec. 7, 2006), the court found the plaintiff’s allegations of unjust enrichment sufficient based
 18 on indirect gain from a third party. In *Kreidler*, the defendant had taken money from a third
 19 party that was intended to pay for insurance provided by the plaintiff. *Id.* at *9. Here, Plaintiff
 20 alleges that “Benefits were conferred on Defendants when they required Plaintiff and the other
 21 member of the Class to purchase two operating systems for one PC in order to use the
 22 Windows XP operating system. These benefits include, but are not limited to: (a) the amounts
 23 paid by Plaintiff and the other members of the Class for an operating system they did not want
 24 to purchase. . . and (b) artificially increased or sustained sales of Windows Vista Business,
 25 Windows Vista Ultimate, Windows 7 Professional, and/or Windows 7 Ultimate.” (SAC, ¶ 53.)
 26

1 As in *Cardizem*, *Muehlbauer* and *Kriedler*, the allegations in Plaintiff's Second Amended
2 Complaint in this case satisfy the first element of an unjust enrichment claim.

3 2. Microsoft is Aware that it Benefits from its Unfair Scheme

4 Microsoft knows and appreciates that it has benefitted from mandating that consumers
5 purchase Vista or Windows 7 in order to obtain Windows XP. Every consumer purchase of a
6 Vista or Windows 7 license for the purpose of downgrading to Windows XP results in more
7 money in Microsoft's corporate coffers. Indeed, Microsoft includes in its sales figures for
8 Vista the licenses that have been purchased and downgraded to Windows XP. (SAC, ¶28.)

9 3. Microsoft Unjustly Retained Monies Paid by Consumers for Operating Systems
10 They Did not Want

11 It would be unjust to permit Microsoft to take advantage of Plaintiff (and millions of
12 other consumers) by pocketing the proceeds resulting from the forced sale of Vista. Although
13 Microsoft claims that Plaintiff essentially "got what she paid for" because she received full
14 value for her purchase of two operating systems, Microsoft's argument rings hollow. While
15 Plaintiff may have received the two operating systems that she was forced to pay for, she never
16 wanted or needed the Vista operating system in the first place.

17 In summary, the allegations in Plaintiff's Second Amended Complaint are more than
18 sufficient to plead the three elements of an unjust enrichment claim under Washington law. *See*
19 *Cardizem*, 105 F. Supp. 2d at 670-71; *Muehlbauer*, 431 F. Supp. 2d at 854; *Kriedler*, 2006 WL
20 3539005 at *9; *Orient Maritime Ltd. v. SSA Int'l, Inc.*, No. C05-1100L, 2005 WL 3448068, at
21 *1 (W.D. Wash. Dec. 14, 2005). Accordingly, Microsoft's motion to dismiss Plaintiff's unjust
22 enrichment claim should be denied.

23 **D. Plaintiff Has Stated A Claim For Declaratory Relief**

24 Microsoft's argument for the dismissal of Plaintiff's claim for declaratory relief rises
25 and falls with its arguments directed to Plaintiff's CPA and unjust enrichment claims.
26 Microsoft does not assert that the practice that is the subject of this lawsuit has been

1 discontinued such that declaratory relief is unnecessary. In fact, Microsoft has extended its
2 practice from Vista to Windows 7, all the while maintaining that its practice is lawful and
3 proper. Therefore, Microsoft's motion to dismiss Plaintiff's independent claim for declaratory
4 relief under the Declaratory Judgment Act should and must be denied.

5 **V. CONCLUSION**

6 For all of the foregoing reasons, the Court should deny Microsoft's motion to dismiss.

7 DATED this 4th day of December, 2009.

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CERTIFICATE OF SERVICE

I, Beth E. Terrell, hereby declare that on December 4, 2009, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to the following:

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